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BEFORE THE
DEPARTMENT OF TRANSPORTATION
WASHINGTON, D.C.

DEPARTMENT OF TRANSPORTATION

97 FEB 20 PM 4:19

DOCKET SECTION

AMERICAN AIRLINES, INC. et al.
and THE TACA GROUP RECIPROCAL
CODE-SHARING SERVICES PROCEEDING

OST-96-1700 -12

Applications of

AMERICAN AIRLINES, INC.
AVIATECA S.A.
COMPANIA PANAMENA DE AVIACION, S.A.:
LINEAS AEREAS COSTARRICENSES S.A. :
NICARAGUENSE DE AVIACION S.A.
TACA INTERNATIONAL AIRLINES S.A.
TACA DE HONDURAS S.A. DE C.V.

OST-96-1518 -17
OST-96-1511 -17
OST-96-1515 -17
OST-96-1520 -18
OST-96-1513 -17
OST-96-1512 -17
OST-96-1514 -17

for exemptions under 49 USC 40109

Joint Application of

AMERICAN AIRLINES, INC. et al.
and THE TACA GROUP

Undocketed

for statements of authorization under
14 CFR Parts 207 and 212

Application of

AMERICAN AIRLINES, INC.

OST-97-2081 -8

under 49 U.S.C. § 40109 for exemption
(U.S.-Colombia and Route Integration)

Application of

AEROVIAS NACIONALES DE
COLOMBIA, S.A.

for an exemption from 49 U.S.C. § 41301 :

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OST-97-2083' 8

Joint Application of

AMERICAN AIRLINES, INC. and
AEROVIAS NACIONALES DE
COLOMBIA, S.A. ("AVIANCA")

for Statements of Authorization under
14 C.F.R. Parts 207 and 212 (Reciprocal :
Code-Sharing Services) :

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:
Undocketed

MOTION FOR LEAVE TO FILE AND COMMENTS OF THE CITY
OF HOUSTON AND THE GREATER HOUSTON PARTNERSHIP

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February 20, 1997

Application of

AEROVIAS NACIONALES DE
COLOMBIA, S.A.

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OST-97-2083
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for an exemption from 49 U.S.C. § 41301 I

Joint Application of

AMERICAN AIRLINES, INC. and
AEROVIAS NACIONALES DE
COLOMBIA, S.A. ("AVIANCA")

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Code-Sharing Services) :

MOTION FOR LEAVE TO FILE AND COMMENTS OF THE CITY
OF HOUSTON AND THE GREATER HOUSTON PARTNERSHIP

MOTION FOR LEAVE TO FILE

The City of Houston and the Greater Houston Partnership ("Houston" or "Houston Parties") herewith move for acceptance by the Department of the Comments submitted below concerning applications filed in the captioned proceedings. These comments are submitted at this time because information submitted in the Answers of Continental Airlines and United Airlines in Dockets 97-2081 and 97-2083 reveals that American Airlines' two code sharing applications in these dockets are part of a broad effort by American to establish code sharing arrangements with the

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principal foreign flag airline of almost every country in Latin America. The Houston Parties had not been aware of that.

As shown below in Houston's comments, if these two sets of code sharing applications are, in fact, part of a hemispheric program of alliances between American Airlines and its foreign competitors, serious adverse consequences are in store for airline service at Houston and between U.S. and Latin America generally. Considering these circumstances, the Houston Parties respectfully request that the following comments be accepted for consideration as part of the record in these proceedings.

COMMENTS OF THE HOUSTON PARTIES

- A. American's program of marketins asreements in Latin America is highly anticompetitive.

In its Answer to the applications of American and Avianca, Continental states that American has not only reached marketing/code sharing agreements covering the captioned applications, i.e., with Avianca, the Colombian airline, and with TACA (El Salvador), Aviateca (Guatemala), LACSA (Costa Rica), NICA (Nicaragua), and COPA (Panama), but that American has made or is pursuing similar agreements with a number of other foreign flag competitors in the region. These include Aerolineas Argentinas, LAPSA (Paraguay), SAETA (Ecuador), Iberia (which serves Central and South America and owns interests in South

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American carriers), LanChile (Chile), Pluna (Uruguay), Varig (Brazil), and Viasa (Venezuela). Continental's Answer goes on to point out that American "already controls the majority of U.S. flag seats in virtually every South American country and its potential partners control the majority of foreign-flag nonstop seats in the market." (Answer of Continental, Dockets 97-2081, and 97-2083, p. 6). In short, the dominant U.S. airline in Latin America is systematically creating code share alliances in the region which are designed to give it even greater market power, especially in markets subject to capacity restrictions. Such market power is unlikely to abate even where the U.S. is able to negotiate "open skies" agreements. First, an open skies agreement would undoubtedly trigger a request by American and its foreign partner for the same anti-trust immunity the U.S. has granted to marketing agreements with open skies partners in Europe. If granted, such immunity would further assure the domination of Latin American service by American.

In any case, the partnerships American is creating throughout the continent are unlikely to face serious new competition where bilateral agreements become more liberal. U.S. airline deregulation, despite its overall success, teaches that, when it comes to airline competition, size matters. Large route systems with vast feeder networks have an inherent competitive

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advantage not easily matched by newcomer airlines." If American with its overwhelming size in Latin America succeeds in creating the partnerships that Continental has identified, it will have enough size and traffic feed between itself and its code share partners to discourage the most optimistic potential competitors.

Although the Department has approved many code sharing agreements, and in some cases has granted anti-trust immunity, it has not concluded that such agreements, even in an open skies environment, can never be anti-competitive. The dark side of code sharing was illuminated in the Study of International Airline Code Sharing prepared for the Department by GRA Incorporated and submitted in December, 1994. The text of the GRA Report includes these observations (at p. 45):

If the code-sharing partners are the only ones offering "online" service in thin markets, they may be able to utilize their market power to extract monopoly rents. In such situations, any agreement for code sharing or service coordination could reduce competition by allowing competitors to essentially engage in a market-sharing arrangement that restricts flight offers. In

^{1/} American's marketing agreements could also have the perverse effect of discouraging certain countries from considering liberalization of their agreements with the U.S. This would occur most probably in countries where American's partner is closely enough affiliated with its government to argue persuasively that significant increases in capacity in U.S. markets are contrary to the government's interest.

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practice, then, the overall net welfare impacts may depend significantly on the nature of existing competition in the city-pair market in question.

The potential for anti-competitive behavior is presumably somewhat less in more competitive, larger markets where more than one carrier offers comparable service. In such markets, the discipline imposed by competition may inhibit code-sharing partners from extracting supra-normal profits from their code-sharing flights. On the other hand, if the partners were the primary competitors prior to a code-sharing agreement, the overall impact on market welfare could be adversely affected." (emphasis added)

American's program of creeping cartelization throughout Latin America is far bolder and more expansive than worst case scenarios discussed by GRA. For the sake of competition and consumers, the time to address this new scenario is now.

- B. American's marketing agreement program, if successful, would seriously weaken Houston as a gateway and Continental as a competitor in service to Latin America.

In several recent proceedings the Department has made clear that it recognizes the need for additional competition in U.S. airline service to Latin America and that it sees the strengthening of Continental's Houston gateway as an important means to that end. For example, in U.S.-Colombia Combination Service Case, Order 93-9-12, where Continental's Houston gateway

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proposal was chosen over a proposal by United for additional service to Colombia from Miami, the Department declared:

By serving a new gateway, Continental's proposal offers travelers a significant alternative to existing services in the U.S.-Colombia market and thus promotes intergateway competition. In addition, the selection of Continental would promote the development of a third significant U.S.-flag competitor in South America. (Order 93-9-12, p. 7)

More recently, in the U.S.-Lima Combination Service Proceeding (1996), the Department again emphasized the importance of the Houston gateway by selecting Continental's Houston proposal over American's Dallas/Ft. Worth gateway proposal. The Department found (Order 96-4-48 at p. 8):

Our tentative selection of Continental over American would most enhance intergateway as well as intercarrier competition in the U.S.-Lima market. Our own review of American's proposal agrees with Continental that nearly 60 percent of American's proposed Dallas/Fort Worth traffic comes from cities that American already serves on its Miami-Peru nonstop service. American's proposal would thus offer far less intergateway competition than would Continental's proposal. Unlike American, Continental has a strong incentive to offer a competitive alternative to the Miami gateway from Houston through aggressive pricing as well as improvements in service. With both an eastern and a western gateway, Continental will offer strong competition to

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the national coverage of both American and
United out of Miami.^{2/}

American's code share offensive throughout Latin America is an effort to obtain indirectly what the Department has rejected directly: the domination of Texas gateway service to Latin America by the same airline that dominates Florida gateway service. American already possesses, by virtue of a broad route description, abundant nonstop authority between DFW and key points in Latin America. However, American's DFW service does not have a large pool traffic to call upon without self diverting traffic from its Miami service. Nor is American able to access significantly more behind gateway traffic of DFW than Continental at Houston.

Code sharing agreements between American and its foreign flag competitors could change this by funnelling more foreign originating passengers, moving under a foreign flag code, to the DFW gateway. American's access to this traffic would in part be at the expense of Houston gateway service, thus making it possible to sustain both DFW and Miami as American Airlines'

^{2/} See also the recent decision in the U.S.-Peru Combination Service Proceeding, Order 95-10-24, where the Department selecting Continental for additional frequencies, stated that the "heavily concentrated nature of the U.S.-flag service in the market has created a strong public need for new entry, price/service options, and competition." p. 6.

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gateways and weakening, in some cases fatally, Continental's nascent Houston gateway service.

Such an outcome is plainly American's goal. It is, of course, exactly the opposite of what the Department has been trying to achieve in cases such as Colombia and Lima. It would suffocate the intergateway competition the Department foresaw in Houston service and, by allowing American to create DFW as the dominant Texas gateway to Latin America, would assure that no Texas gateway serves as a competitive spur to American's huge operation at Miami.

American's effort to checkmate competition from Houston to Latin America is a perfectly rational strategy for it. The time has come, however, for the Department to measure that strategy against the public interest and act to assure truly adequate service and competition in underserved and overpriced U.S.-South America markets.

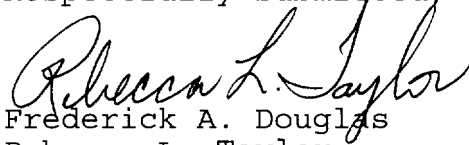
This is not, unfortunately, a matter the Department is free to consider at leisure. American's current high market shares, combined with its current code sharing offensive, have apparently already convinced many Latin American airlines that their only chance of survival against the "900 pound gorilla" from the north is by leaping into its arms. In some cases, Houston is advised, American's would-be partners are already funneling traffic to it in anticipation of favorable DOT action.

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C. Conclusion

Under all the circumstances, the Department should announce promptly that it will withhold its approval of the applications in the captioned matters until it has before it American's entire program for code sharing with foreign flag competitors in Latin America (including the Caribbean). The Department should then address itself to the competition issues raised by that program in its entirety. In the meantime, it should caution American and its potential foreign flag partners against any de facto joint action which would be injurious to competition by other U.S. flag airlines.

Respectfully submitted,

A handwritten signature in cursive script, reading "Rebecca L. Taylor".

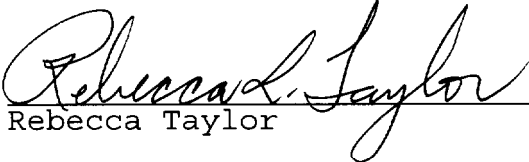
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Comments of the City of Houston
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CERTIFICATE OF SERVICE

I hereby certify that I have this 20th day of February, 1997, caused to be served a copy of the foregoing Motion For Leave To File And Comments of the City of Houston and the Greater Houston Partnership by United States mail, first-class, postage prepaid in accordance with the Department's regulations to the persons listed on the attached service list.


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